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No. 03-604

Supreme Court, U.S.
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In The

Supreme Court of the United States

CIRCUIT CITY STORES, INC.,

Petitioner,

v.

CATHERINE INGLE,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

MICHAEL H. CROSBY
Counsel of Record
D.F. Garrettson House
2366 Front Street
San Diego, California 92101
(619) 696-7330

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OR CALL COLLECT (402) 342-2831

I. QUESTION PRESENTED

Whether the Ninth Circuit correctly held that an arbitration agreement in an employment contract is unconscionable when i) the employee could not opt out of arbitration or negotiate the terms of arbitration; ii) the agreement to arbitrate expressly bound only the employee, not the employer; and iii) the agreement required arbitration under rules written by the employer that truncated important procedural rights and substantive remedies.

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BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

II. INTRODUCTION

Petitioner Circuit City Stores, Inc. ("Petitioner" or "Circuit City") brings this case, filed by Catherine Ingle ("Respondent" or "Ms. Ingle") in early 1999, to this Court for the second time on an interlocutory matter.

Petitioner asks this Court to grant certiorari to establish as law a statutory interpretation that no state or federal circuit has tested. That is, when a state applies its common law or statutory rules of contract, as it must do pursuant to 9 U.S.C. § 2, the Federal Arbitration Act ("FAA") § 2, it must apply those rules differently to arbitration agreements, forgiving deficiencies that would invalidate other types of contracts. This Court has declined certiorari in other cases raising the FAA preemption issue, including the closely-related case of *Circuit City Stores, Inc. v. Adams*, 279 F.3d 889, *cert. den.*, 532 U.S. 938 (2002). This petition is still premature. Moreover, the proposed rule would intrude unjustifiably into a province reserved to the states: the law of contract.

California applies the two-pronged unconscionability test to all contracts, rejecting only those contracts characterized by procedural and substantive one-sidedness. If the Ninth Circuit has misconstrued California law of unconscionability, as Petitioner suggests, it is a mistake for the Supreme Court of the State of California to correct, not the Supreme Court of the United States.

III. STATUTES INVOLVED

The Federal Arbitration Act, 9 U.S.C. § 2, provides:

> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, *save upon such grounds as exist at law or in equity for the revocation of any contract*.

California Civil Code ("CC") § 1670.5(a) reads:

> (a) If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

IV. STATEMENT OF THE CASE

A. Factual Background

Ms. Ingle applied for the position of sales associate at Circuit City in San Diego, California in September 1996. At the time of application, she was given forms and told where to sign. Ms. Ingle was not given an opportunity to read the forms she was told to sign. She never was offered the opportunity to "opt-out" of the compulsory arbitration

program. She never was given the opportunity to negotiate any term of the agreement.

Ms. Ingle was not shown any dispute resolution rules; no one in management explained them to her. She never saw the rules contained in Circuit City's Dispute Resolution Agreement ("DRA") at any time she worked on the job. She was never advised of any changes in the rules.

Ms. Ingle twisted her back at work helping to transport a wide-screen television in December 1997. She was placed on a five-week leave of absence. At about that time, her supervisor Keith Anderson, whose sexual advances toward Ms. Ingle approached stalking, became angry that she had rejected him. When Ms. Ingle returned to work in January 1998, she presented Anderson with a doctor's written instructions that her work hours and lifting be limited strictly. Anderson, though, assigned her to work up to 60 hours in a week, with heavy lifting. Ms. Ingle reported the harassment to store manager Eric Gibbs. His statements, actions and inactions caused further and far greater damage, so Ms. Ingle reported the harassment to Circuit City through its purportedly confidential "cool-line." Cool-line personnel immediately contacted Mr. Gibbs, and he confronted Ms. Ingle in an angry and threatening manner. Soon thereafter she contacted Circuit City's Western Regional Manager. No one at Circuit City responded to her report by informing Ms. Ingle of the dispute resolution rules. No one gave her a claim form to file.

Ms. Ingle retained an attorney, her counsel of record. Circuit City's in-house attorney sent a copy of its purported dispute resolution rules in mid-April 1998. Ms. Ingle's counsel contacted the two leading alternative

dispute resolution providers in San Diego, J.A.M.S./ Endispute ("J.A.M.S.") and AAA. He provided them with copies of Circuit City's arbitration agreement and rules. He inquired whether either firm would administer an arbitration under those rules. Both neutral providers refused to administer arbitration under Circuit City's one-sided rules.

B. Procedural History

Plaintiff filed her Complaint for Sexual Harassment [California Government Code ("Gov.C.") § 12940(h)]; Failure to Prevent Sexual Harassment [Gov.C. § 12940(i), (h)(3)]; Unlawful Employment Discrimination on the Basis of Gender or Physical Handicap [Gov.C. § 12940(a)]; Retaliation for Protesting Sexual Harassment [Gov.C. § 12940(f)]; Failure to Reasonably Accommodate Physical Handicap [Gov.C. § 12940(k)]; Gender Discrimination and Harassment [42 U.S.C. § 2000e]; Retaliation for Reporting Employment Discrimination [42 U.S.C. § 2000e] on June 21, 1999.[1] No answer has been filed by Petitioner. Defendant filed a motion to compel arbitration on July 16, 1999. The motion was based in part on the Declaration of Pamela Parsons and Exhibits A and B thereto. Plaintiff filed her response on August 16, 1999. The opposition was supported by declarations by attorney Michael Crosby (with exhibits) and Catherine Ingle.

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[1] A prior, more limited version of this complaint (Case No. 99 CV 0181J JFS) was filed on March 3, 1999 and dismissed for lack of subject matter jurisdiction on May 24, 1999.

The motion was heard and denied by the late Honorable Edward J. Schwartz on August 30, 1999. (Transcript of Hearing, 8/30/99, is Appendix 1.) A written order was signed on September 21, 1999 and entered September 22, 1999.

Defendant filed its notice of appeal on October 5, 1999. Respondent filed her motion to dismiss the appeal on November 19, 1999. The motion to dismiss was granted on January 24, 2000.

Petitioner sought a writ of certiorari which this Court held, then granted on March 26, 2001 after it ruled in *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105 (2001).[2]

After renewed briefing, on May 23, 2003 the Ninth Circuit filed its decision affirming the District Court's denial of Petitioner's motion to compel Respondent's claims to arbitration. (*Ingle v. Circuit City Stores, Inc.*, 328 F.3d 1165 (9th Cir. 2003).)

Petitioner filed a motion for rehearing that was denied on July 8, 2003. This petition followed.

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[2] *Adams* was remanded and the Ninth Circuit found an essentially identical version of the DRA to be unconscionable. *Circuit City Stores, Inc. v. Adams*, 279 F.3d 889 (9th Cir. 2002). Circuit City petitioned this Court for writ of certiorari. Certiorari was denied (532 U.S. 938). The *Adams* petition presented two questions, one of which was the same in essence as the question presented here and in the petition filed in *Circuit City Stores, Inc. v. Mantor*, No. 03-605, to reverse *Mantor v. Circuit City Stores, Inc.*, 335 F.3d 1101 (9th Cir. 2003).

C. Lower Court's Analysis of the Document in Issue

The appellate court rested its decision to affirm on its determination that the 1998 version of the arbitration agreement was unconscionable under state law.[3] The court identified one DRA "rule" after another that was so oppressive that the agreement overall was substantially unconscionable: (1) it bound employees, but not the employer, to arbitrate claims (Pet.App. 10a-14a and footnote 5); (2) the statute of limitations was too restrictive, and would deprive discrimination claimants like Ms. Ingle of the benefit of the continuing violation doctrine (Pet.App. 14a-15a); (3) it prohibited class actions (Pet.App. 15a-17a); (4) it required even indigent claimants to pay a fee to Circuit City to initiate the claim (Pet.App. 18a-19a); (5) it required the employee to pay the employer's attorneys fees and costs if she failed to prove her claims (Pet.App. 19a-21a); (6) it truncated or denied remedies, including injunctive relief, full back-pay, adequate front pay, compensatory damages equivalent to those available in court, and punitive damages over $5,000 or an amount based on the pay award (Pet.App. 21a-22a); (7) it gave Circuit City the unilateral right to modify or terminate the agreement, or any of its terms, including the rules (Pet.App. 22a-23a); so (8) it was so pervasively oppressive that the unfair provisions could not be severed without a complete redrafting of the contract by the court (Pet.App. 23a-26a).

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[3] Petitioner attached the 1998 DRA as an exhibit to the declaration of Pamela Parsons in support of the motion to compel arbitration.

The Circuit City DRA the Ninth Circuit reviewed fails utterly to meet this Court's standard of fairness, and its requirement that employees receive the full benefit of the laws, whether in open court or closed arbitration. (*See Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 26, 111 S.Ct. 1647 (1991).) Given the manifold provisions that deny Petitioner's employees substantive rights guaranteed by law, Petitioner's agreement fails to measure up to standards established firmly by this Court.

V. REASONS THIS PETITION SHOULD NOT BE GRANTED

A. No Actual Dispute Exists Concerning the Construction of FAA Section Two's Savings Clause

A petition for writ of certiorari will only be granted where a case involves a federal question of general importance or where there is a split among circuit courts of appeal. (*See* 28 U.S.C. §§ 1254, 1257; *Fields v. United States,* 205 U.S. 292 (1970).) Petitioner here argues mistakenly that a split exists among the lower courts regarding the question of when state law rules that would invalidate an arbitration agreement are preempted under FAA Section 2. Specifically, Petitioner admits that the Ninth Circuit, Second Circuit and California Supreme Court hold that state law rules such as the doctrine of unconscionability fall within the category exempted from preemption by FAA Section 2. However, in a strained effort to identify opposition to the Ninth Circuit, Second Circuit and California Supreme Court views, Petitioner concludes, without citing a single case in actual support of its proposition, that the First Circuit, Third Circuit and Alabama Supreme Court hold a contrary view. Petitioner contends

that these courts conduct a sort of self-critical assessment to assure that when it applies that state's doctrine of unconscionability to an arbitration agreement, it does not apply that law in an arbitration-specific manner.

This is not the law as declared by this Court in *Perry v. Thomas*, 482 U.S. 483 (1997) or *Doctor's Associates, Inc. v. Casarotto,* 517 U.S. 681 (1996). Those opinions require that no statutes be written to regulate arbitration agreements alone, as the California and Montana statutes in *Perry* and *Casarotto*, respectively, were directed. At its broadest, this Court in *Perry*, at footnote 9, requires that contract law of general application, such as the rule of unconscionability, may not be used to invalidate arbitration agreements simply because such agreements compel disputants to present their claims to an arbitrator rather than a judge.

The opinion in *Ingle* does not offend the *Perry/ Casarotto* principle, and it does not conflict in a jurisprudentially-significant manner with the three principal cases cited by Petitioner.

1. The *McNaughton* Case

Petitioner's argument in support of preemption is facially inconsistent and seeks to fabricate a conflict among the state and lower courts that does not exist. Specifically, Petitioner argues incorrectly that the Alabama courts imply an extra analytical step not required by the express saving clause of Section 2. The rule Petitioner perceives would require a court to determine whether a generally applicable state law rule of contracts is applied in an arbitration-specific manner. However, the exact opposite is true under Alabama law. Alabama courts

concur with the Ninth Circuit, Second Circuit and the California Supreme Court, holding that "state law, as it applies generally to all contracts, may be applied to test validity, revocability, and enforceability of particular arbitration agreements under FAA." (*Young v. Jim Walter Homes, Inc.*, 110 F.Supp.2d 1344 (M.D. Ala. 2000).) Generally-applicable state contract defenses such as fraud, duress or unconscionability may be applied without conflict with the FAA. (*General Motors Corp. v. Stokes*, 2003 WL 22419473 (Ala. 2003).)

The Alabama Supreme Court opinion in which Petitioner divines the clearest articulation of the principle it advances, *Ex parte McNaughton*, 728 So.2d 592 (Ala. 1998), does not support its construction of Section 2 at all. Plaintiff in *McNaughton* brought a claim for fraud and interference with business relations. Employer moved to compel arbitration, and the motion was granted. The Alabama Supreme Court, in a 5-4 opinion, disavowed what the majority characterized as dictum in *Northern, Ltd. v. James*, 694 So.2d 1329, 1338 (Ala. 1997). (*Id.* at 597.)

The *McNaughton* majority noted that the employee had challenged the arbitration on only one basis: "Mutuality of remedy." (*Id.* at 598, n.6.) The *McNaughton* majority noted that under Alabama law the contract doctrines requiring mutuality and those requiring conscionability are "distinct doctrines." As such, *McNaughton*'s holding is not based on unconscionability at all. It merely holds that a contract that requires an employee to arbitrate all legal and equitable claims, but does not bind the employer similarly, is enforceable under Alabama law against a mutuality of remedy challenge.

2. The *Harris* Case

Petitioner finds support for its thesis in *Harris v. Green Tree Financial Corporation*, 183 F.3d 173 (3rd Cir. 1999). *Harris* provides no help. The Third Circuit applies federal unconscionability law. Nothing in *Harris* suggests even indirectly that Petitioner's two-step analysis is necessary. At most, it echoes *Casarotto*.

Perhaps the result under California law would differ from that reached under the law of unconscionability applied by Pennsylvania federal and state courts. The result is of no consequence. The question is whether the Third Circuit (and Pennsylvania) applies the same test as the Ninth Circuit (and California). It appears that it does. The conflict Petitioner perceives is an illusion.

3. The *Securities Industry Association* Case

Finally, Petitioner submits that *Securities Industry Association v. Connolly*, 883 F.2d 1114 (1st Cir. 1989) buttresses its position. It does not. This opinion considers whether "certain regulations, Mass.Regs.Code tit. 950, §§ 12.204(G)(1)(a)-(c) (Regulations) . . . are preempted by the FAA." (*Id.*, 883 F.2d at 1116.) The Regulations governed the conduct of securities sales within the Commonwealth of Massachusetts. Specifically, it examined provisions of the Regulations addressing directly what securities brokers must do with respect to voluntariness, conspicuousness and disclosure of the legal effect of predispute arbitration agreements. (*Id.* at 1117.)

Such express limitations on arbitration agreements are precluded clearly by *Perry v. Thomas* and *Doctor's Associates v. Casarotto*.[4] *Securities Industry Associates* does not address any of the "grounds as exist at law or in equity for the revocation of any contract." (FAA § 2.) There is no conflict here that rises to the level at which Supreme Court review is appropriate. Indeed, the opposite is true. More states and circuits must weigh in on the issue Petitioner presents before it is ripe for debate in this Court.

It is indeed possible that California courts or the Ninth Circuit interpreting California law would decide that Civil Code § 1670.5 would preclude enforcement under *McNaughton*'s facts. However, that only proves that Alabama courts may apply to common law of mutuality of obligation in a way that occasionally produces results different from those that might occur when California courts apply CC § 1670.5. That is not necessarily bad. It is implicit in the philosophy of federalism and, indeed, the saving clause of FAA Section 2.

4. No Court Has Endorsed Petitioner's Self-Serving Interpretation of FAA Section Two

Petitioner acknowledges that "Section 2 of the Act requires state and federal courts to enforce arbitration agreements as they would any other contract." *(See* Petitioner's Brief, page 4.) Petitioner attempts to reconstruct

[4] In fact, the Regulations are similar in effect to the statutes this Court struck down in *Perry v. Thomas* and *Casarotto*.

the express exemption provision of Section 2 to require lower courts to conduct an extra inquiry to determine whether the otherwise unambiguous exemption applies *differently* and *less favorably* to pre-employment arbitration agreements than any other agreements. What Petitioner is really asking this Court is to rewrite the FAA to direct lower courts *not* to treat arbitration agreements as they would *any other contract*, as the law currently mandates.

No Circuit or state court has endorsed the interpretation Petitioner advances. Neither the State of Alabama nor the Third Circuit calls for a special interpretation of arbitration agreements. Contrary to Petitioner's argument, the Third Circuit is in line with the Ninth Circuit, the Second Circuit as well as the California Supreme Court. The Third Circuit requires that its courts evaluate general state law doctrines such as unconscionability in the context of arbitration agreements the way they would evaluate application of such doctrines with *any other contract*. (*Blair v. Scott Specialty Gases,* 283 F.3d 595, 603 (3rd Cir. 2002) (a federal court must generally look to the relevant state law on the formation of contracts to determine whether there is a valid arbitration agreement under the FAA); *Harris v. Green Tree Financial Corp., supra,* 183 F.3d at 178 (arbitration agreements are placed upon the same footing as other contracts and are only enforceable to the extent as other contracts are enforceable).)

Similarly, the First Circuit agrees that arbitration agreements are to be afforded no more or no less protection than *any other contract*. (*See DiMercurio v. Sphere Drake*, 202 F.3d 71, 80-81 (1st Cir. 2000) (arbitration agreements are enforceable except in circumstances that would invalidate any other contract; one-sided agreements

to arbitrate are not favored).) Thus, it is apparent why Petitioner failed to cite to any case authority directly supporting its construction of FAA Section 2 from the First Circuit, Third Circuit, or Alabama courts: there is none.

B. Cases Applying Cal. Civ. C. § 1670.5 to Arbitration Agreements Balance Competing Public Interests

Petitioner in effect asks this Court to order California's courts to interpret the state's own statutes differently. The California Arbitration Act (California Code of Civil Procedure ("CCP") §§ 1281-1294.2), like the FAA, 9 U.S.C. §§ 1-16, is construed to favor arbitration. Since the FAA defers construction of the contract defenses in the saving clause of Section 2 to state law (*see First Options of Chicago v. Kaplan*, 514 U.S. 938, 944, 115 S.Ct. 1920), the state and federal policies favoring arbitration must be balanced against the policy permitting enforcement of only those contracts that are formed without duress, deceit or undue influence, and are not unconscionable.

California's Supreme Court has struggled to balance these public policies in a number of contexts, including consumer credit, real estate and mortgages, medical malpractice and, as here, pre-employment arbitration agreements. The court struck that balance in the compulsory pre-employment arbitration context in *Armendariz v. Superior Court*, 24 Cal.4th, 6 P.2d 669 (2000) and *Little v. Auto Stiegler, Inc.*, 29 Cal.4th 1064, 63 P.3d 979, *cert. den.*, 124 S.Ct. 83 (2003).

Petitioner would prefer that California would strike this balance other than it did in *Armendariz*. It petitions

this Court to order California to weigh the respective policies differently. This Court should decline, as it typically does, to re-order state policy choices by fiat.

C. The law to be applied to determine whether a contract is unenforceable for unconscionability is the state law applicable to contracts generally

(*Doctor's Associates, Inc. v. Casarotto, supra*, 116 S.Ct. 1652 (1996).)

> Repeating our observation in *Perry* [*v. Thomas*, 482 U.S. 483, 107 S.Ct. 2520 (1987)], the text of § 2 declares that state law may be applied "if that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally." [Citation.] Thus, generally applicable defenses, such as . . . unconscionability, may be applied to invalidate arbitration agreements without contravening § 2. [Citations.]
>
> Courts may not, however, invalidate arbitration agreements under state laws applicable *only* to arbitration provisions. [Citation.]

517 U.S. at 686-687, 116 S.Ct. at 1656. Thus, the FAA *requires* that state law principles be applied to assess the enforceability of this agreement.

In fact, *Casarotto* was relied on in a case decided recently by the Ninth Circuit. In *Ticknor v. Choice Hotels Int'l. Inc.*, 265 F.3d 931 (9th Cir. 2001), this court overruled precedent set in *Cohen v. Wedbush, Noble, Cooke, Inc.*, 841 F.2d 282 (9th Cir. 1988) and *Bayma v. Smith, Barney, et al.*, 784 F.2d 1023 (9th Cir. 1985), for the contrary proposition that state law principles may not be applied in a case governed by the FAA. The court in

Ticknor found those decisions to conflict with this Court's holding in *Casarotto* that under the FAA, "generally applicable [state law] contract defenses, such as fraud, duress, or unconscionability, may be applied to invalidate arbitration agreements without contravening [9 U.S.C.] § 2." *Ticknor, supra,* 265 F.3d at 937. It stated:

> The Supreme Court's decision in *Doctor's Associates* [*v. Casarotto*] does, however, cause us to reconsider our prior decision in *Cohen* . . . and *Bayma*. . . . Because certain aspects of *Cohen* and *Bayma* cannot be reconciled with [*Casarotto*], we must overrule them insofar as they hold that state law adhesion contract principles may not be invoked to bar arbitrability of disputes under the Arbitration Act.

Id. at 941-942.

California courts treat mandatory arbitration contracts no differently from other similar contracts. That is because California law (CCP §§ 1281 *et seq.*) and public policy favor the enforcement of arbitration agreements. California's strong policy favoring arbitration has been noted affirmatively as being in conformity with the strong federal policy favoring arbitration of disputes. (*Reiss v. Murchison*, 384 F.2d 727, 734 (9th Cir. 1967).)

D. The Ninth Circuit Enforces Employment Arbitration Agreements That Demonstrate a Modicum of Bilaterality or Where Circumstances Show That the Employee Had a Meaningful Opportunity to Choose

Petitioner's argument boils down to the proposition that the Ninth Circuit in *Ingle* "effectively establish[ed] a

new rule that all mandatory employment arbitration agreements are presumptively unconscionable." (Pet. Brief at 9.) This characterization is wrong.

The Ninth Circuit has upheld *non-mandatory* arbitration agreements against unconscionability challenges. The most obvious refutation of Petitioner's proposition is found by contrasting *Ingle* and *Mantor* with two other Ninth Circuit cases examining Circuit City's DRA, *Circuit City Stores, Inc. v. Najd*, 294 F.3d 1104 (9th Cir. 2002) and *Circuit City Stores, Inc. v. Ahmed*, 283 F.3d 1198 (9th Cir. 2002).[5]

Briefly stated, in *Najd* and *Ahmed* the employees had a meaningful opportunity to accept or reject the arbitration program. They did not reject it. The Ninth Circuit compelled both employees to arbitrate their claims, even though they would be required to do so under the same oppressive rules detailed in the *Ingle* and Ninth Circuit *Adams* opinions.[6]

As *Ingle* frames the rebuttable presumption of substantive unconscionability, it requires three findings: (1) the employer made the provision a mandatory prerequisite to employment; (2) the employee had no meaningful opportunity to negotiate its terms; and (3) the agreement binds only the employee, not the employer, to negotiate. (*Ingle* at 13a.)[7] The employer may then present evidence

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[5] These cases are discussed in the Brief in Opposition filed in the *Mantor* case, No. 03-605.

[6] *See also, Ticknor, supra,* 265 F.3d at 939-940.

[7] Contrary to Petitioner's suggestion that the 1998 DRA is not expressly limited to "Associates"; the contract states, *inter alia*, that it

(Continued on following page)

that the provisions are fair. If they are, the contract will be enforced.

In this particular case, the court analyzed a mandatory agreement that was so oppressive that it could not be remedied, only rewritten. It contained limits on the time in which claims could be brought, severe limits on remedies; an intimidating cost-shifting provision that contravened established employment discrimination law; and, overall, it placed near-total control over employment dispute resolution in the hands of the employer.

Almost all arbitration agreements are more fair than Petitioner's. The great majority of arbitration agreements are enforced in California. Nothing in the *Ingle* opinion prevents the enforcement of reasonably fair arbitration agreements arrived at in a reasonable manner.

E. California's Unconscionability Statute Applies Consistently to A Wide Array of Contracts

1. The Test To Identify Procedural Unconscionability In *Ingle* Is Applied To Contracts of All Sorts

Petitioner argues at page 4 that the test of procedural unconscionability, focusing on inequality of bargaining power and the presence or absence of a meaningful opportunity to negotiate contract terms, "would apply in almost

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applies only to "any and all employment-related legal disputes, controversies or claims *of an associate*." (*Id.* at 11a.)

all employment situations." This is true only when employers have no meaningful opportunity to negotiate contract terms. The courts have acted legitimately and in harmony with the FAA when they have drawn *employment-specific* standards for scrutinizing arbitration agreements.

Civil Code § 1670.5 and court opinions construing it are founded in established common law principles of contract interpretation. The unconscionability doctrine has been "recognized to include an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party." (*Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445, 449 (D.C. Cir. 1965), cited in Farnsworth, *Farnsworth on Contracts* (Supp. 1998) § 4.28, p. 195; *see also* Restatement 2d, *Contracts*, § 208 and *official comments* thereto; Lord, *Williston on Contracts* (4th ed.) § 18.10 (1998) and cases collected therein; UCC 2-302; 1 Witkin, *Summary of California Law* (9th ed.), Contracts §§ 23-26 (1987).

The test to identify adhesion and procedural unconscionability stated in *Ingle* is applied commonly to all contracts – not just arbitration provisions and not just in the employment context. (*See, e.g., Marin Storage & Trucking, Inc. v. Benco Contracting and Engineering*, 89 Cal.App.4th 1042, 1052, 107 Cal.Rptr.2d 645 (2001) (indemnity agreement in commercial contract); *Perdue v. Crocker National Bank*, 38 Cal.3d 913, 925, n.9, 702 P.2d 503 (1985) (bank charges for insufficiently funded checks).) California courts and the Ninth Circuit apply this same test to arbitration provisions in employment contracts. When Petitioner argues that this application is unfair and discriminatory, what it seeks is a special

exemption for employers from the widely-recognized principle that finds contracts imposed by one party on the other on a take-it-or-leave-it basis to be procedurally unconscionable.

2. The Rebuttable Presumption of Substantive Unconscionability Announced In *Ingle* Is Applicable to Various Commercial or Consumer Contract Provisions

The presumption of substantive unconscionability that concerns Petitioner is raised by "a contract to arbitrate between an employer and an employee. . . . " There are two elements that must combine: (i) the arbitration provision imposed without meaningful opportunity to negotiate; and (ii) the employment relationship. This presumption is merely a recognition that the disproportionate negotiating power that inheres in the relationship between employer and employee will most often result in a provision disproportionately favorable to the more powerful party, the employer. The evidentiary burden simply is shifted to the employer to show that whichever party had the power edge and whether the parties actually negotiated the provision or not, the resulting agreement is a fair one.

Petitioner claims that the principle announced in *Ingle* applies only to arbitration agreements, and this offends FAA Section 2. But it is far too early to say that. The presumption may well be adopted by California courts and applied (i) to any contract alleged to be unconscionable; and (ii) to mortgage, banking or other commercial or consumer contracts. After all, the test for substantive unconscionability cited in *Ingle* was articulated first in the

hornbook opinion, *A & M Produce Co. v. FMC Corp.*, 135 Cal.App.3d 473, 486, 186 Cal.Rptr. 114 (1982), a commercial contract case. If the rule originating in a commercial, non-arbitration case may be applied to an employment arbitration case, there is good reason to expect that a corollary of that rule, applied initially in an employment arbitration context, would be applied when circumstances suggest that a non-arbitration provision in a commercial contract resulted from an imbalance in the parties' negotiating power.

The California courts as well as the Ninth Circuit (or other circuits) may well apply the presumption announced in *Ingle* contexts outside of arbitration. It is certainly too early to say they would not. Certiorari based on Petitioner's presumption that *Ingle's* interpretation of California unconscionability law *does and must* conflict with Section 2 of the FAA is thus premature, at best. As this Court has instructed, "generally applicable contract defenses, such as fraud, duress, or unconscionability, may be applied to invalidate arbitration agreements without contravening federal law." (*Doctor's Associates v. Casarotto, supra*, 517 U.S. at 686-687.)

F. California Utilizes Rebuttable Presumptions to Resolve a Variety of Contract Issues

Circuit City notes that the *Ingle* court in its footnote 9 found that a party seeking to enforce a compulsory pre-employment arbitration agreement bears the burden to show that the adhesive provision is substantively fair. Contrary to Circuit City's suggestion, though, such reversed burdens arise in various aspects of California contract law.

In *Jacobs v. Tenneco West,* 186 Cal.App.3d 1413, 1417, 213 Cal.Rptr. 351 (1986), the court considered an established principle of contract performance: "'[w]here a party's breach or non-performance contributes materially to non-occurrence of a condition of one of his duties, the non-occurrence is excused.' (Restatement 2d, *Contracts, supra,* § 245, p. 259)." (*Jacobs, supra,* 186 Cal.App.3d at 1417.) The *Jacobs* appellate panel inferred, then, that in such a case where the condition failed to occur, *the usual burden of proof was reversed,* so that Tenneco West, the breaching party, was required to prove that the condition (approval of the litigated contract by the company's board of directors) would not have occurred even if it had performed its contractual obligations. (*Id.* at 1418.)

In all sorts of contract cases, the burden to prove that damages sought by an innocent, non-breaching party are too uncertain to be recovered is placed on the shoulders of the party who breached the contract. (*See Israel v. Campbell*, 163 Cal.App.2d 806, 816, 330 P.2d 83 (1958); *Brawthen v. H & R Block*, 52 Cal.App.3d 139, 148, 124 Cal.Rptr. 845 (1975); *Mahoney v. Founders Ins. Co.*, 190 Cal.App.2d 430, 12 Cal.Rptr. 114 (1961)).

These commercial contract cases are analogous to mandatory arbitration cases. Once the plaintiff establishes the preliminary fact (failure to perform obligation [*Jacobs*], breach of contract [*Israel, Brawthen, Mahoney*], inequality of bargaining power resulting in adhesive employment arbitration agreement [*Ingle*]), then the presumption arises and the usual burden is reversed. By reversing the burden of proof in the instance of arbitration agreements imposed as a condition of employment, the Ninth Circuit is treating arbitration agreements the same as California treats all contracts.

G. The Decision Below Construing State Law Does Not Discriminate Against Arbitration; It Recognizes The Inequality of Negotiating Power Inherent In the Ordinary Employment Relationship

Contrary to Petitioner's claim (Petitioner's Brief, p. 17, n.11), *Principal Mutual Life Insurance Co. v. Vars, Pave, McCord & Freedman*, 65 Cal.App.4th 1469, 1488-1489, 77 Cal.Rptr.2d 479 (1998), requires mutuality of obligation across a wide array of contracts: "Mutuality of obligation is necessary only in bilateral contracts where there are mutual promises. . . . Problems arise . . . where the promise states a definite obligation, but the promisor has an election to perform or withdraw at its pleasure."[8]

This definition focuses the inquiry on a principal flaw in the Circuit City DRA: Ms. Ingle is bound to arbitrate disputes, but Circuit City may arbitrate, or not, at its pleasure. Since the dispute in *Principal Mutual Life* arises out of a lease agreement, it is apparent that California courts require mutuality of obligation in *all* bilateral contracts, not just pre-employment arbitration agreements.

The unconscionability principles applied in *Ingle* and cases upon which it relied are applied to a wide array of contracts: "profit-shifting" clauses in a commercial lease (*Ilkhchooyi v. Best,* 37 Cal.App.4th 395, 45 Cal.Rptr.2d 766

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[8] Respondent will not attempt to address all the side issues raised by Petitioner. Much of its brief, such as the discussion of cost-shifting in arbitration agreements, is irrelevant to the Question Presented and amounts to a venting of company grievances against the laws of California, a state in which it chooses to do business.

(1995)); automatic rent increase provisions in mobile home leases (*Vance v. Villa Park Mobile Home Estates*, 36 Cal.App.4th 698, 42 Cal.Rptr. 723 (1995)); interest rate provisions in real estate deeds of trust (*Carboni v. Arrospide*, 2 Cal.App.4th 76, 2 Cal.Rptr. 845 (1991)); *See also, A & M Produce v. FMC Corp., supra,* 135 Cal.App.3d at 486).

Each of these cases proposes a test for unconscionability that would apply only to the subject matter of the particular type of contract before that court. For example, in *Carboni,* the court requires an inquiry into the rate of interest to determine whether the rate shocks the conscience. If it does, the provision is substantively unconscionable. (*Carboni, supra*, 2 Cal.App.4th at 81-82.) One cannot apply the same enforcement principle to employment arbitration agreements which contain no rates of interest. That does not suggest that the *Carboni* appellate court was prejudiced against real estate lenders. Yet this is precisely the argument Petitioner posits here: that California courts are biased because they have constructed tests that apply only to employers.[9]

In fact, the *Armendariz* and *Carboni* courts each heeded the California legislature. The Legislative Committee Comment to CC § 1670.5 notes under "Purposes" that the question, always, "is whether, *in light of the general background and the needs of the particular case,*

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[9] Petitioner conflates its arguments, contending that a rule that treats employers differently from other powerful contracting entities amounts to a differing treatment of arbitration agreements. It does not. While prejudice against employers would be unfair and possibly unlawful, it would not necessarily offend FAA Section 2.

the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract." [Emphasis added.]

California courts, and the Ninth Circuit applying directives from California's Supreme Court, have created standards and frameworks specifically to analyze pre-employment arbitration agreements. These principles do not discriminate against employers or arbitration. They do, however, assure consistency in the various courts that must decide whether these provisions in employment agreements, like all contracts, meet the minimum standard of fairness imposed by the legislature.

VI. CONCLUSION

Pre-dispute employment arbitration agreements are alive and well in California. After *Armendariz* and *Ingle*, California employers know what provisions a pre-employment arbitration agreement must contain, and what it must not. Most employers and their legal counsel appreciate this clarity. Without the tests designed specifically to address issues that arise about employment arbitration agreements, drafters of these provisions would be required to guess how courts would apply principles of unconscionability like "meaningful opportunity to negotiate" or "surprise." By developing particularized criteria,

California courts have engaged in an undertaking they have unquestionable authority to pursue.

Respectfully submitted,

MICHAEL H. CROSBY
Counsel of Record
D.F. Garrettson House
2366 Front Street
San Diego, California 92101
(619) 696-7330